

## Vital Signs: have we finally reached 'peak' house prices?

Written by Richard Holden, Professor of Economics and PLuS Alliance Fellow, UNSW

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*Vital Signs is a weekly economic wrap from UNSW economics professor and Harvard PhD Richard Holden (@profholden). Vital Signs aims to contextualise weekly economic events and cut through the noise of the data affecting global economies.*

*This week: house prices in Sydney and Melbourne are cooling, housing approvals are up, and everyone's wondering if Australian banks have been lending too much.*

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In 1956, US geophysicist M. King Hubbert predicted that the rate of petroleum production for a given geographic area follows a hump-shaped curve, and that the world would reach “peak oil” production in 1970.

And, as the figure shows, Hubbert was pretty right about the peak part, not so much about the inevitable decline thereafter. But the reason [“Hubbert Peak”](#) is in the zeitgeist is because once something peaks there is a natural narrative about its secular decline thereafter.



The Hubbert Peak. Red line = predicted Green line = actual. Wikipedia

Perhaps that's why there has been so much focus this week on the possible peak of Sydney housing prices, and even Australian equities. The [CoreLogic hedonic price index](#) was down in May by 1.3% in Sydney and 1.7% in Melbourne.

This was met with some relatively measured responses like that of AMP economist Shane Oliver who tweeted: “May is weak seasonally so exaggerates but the boom is likely over...”

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That seems like an awful lot of faith to put in one datum point. But perhaps Oliver and others are right. And perhaps there is a very happy story where more supply is coming online while demand is being cooled by APRA's crackdown on interest-only loans to investors.

Partially consistent with that happy scenario, the ABS reported that new housing approvals in April were up by 4.4% on a seasonally-adjusted basis, helping claw back some of the 10.3% decline (on revised figures) from the previous month.

On the demand side, however, figures released by the RBA on Wednesday showed investor credit up 0.6% on a seasonally-adjusted basis in April – a rate of growth unchanged from March. That put annual growth at 7.3%. If APRA's measures have given investors pause then it doesn't seem to have filtered through to the data yet.

Altair Asset Management chairman Philip Parker was worried not only about the housing market, but the ASX as well. In a remarkable decision, Altair announced that it “was to sell all the underlying shares in the Altair unit trusts and to then hand back the cash to those same managed fund investors”.

This sort of thing doesn't happen every day – particularly by a fund manager with a 30-year track record. Or, as Parker put it: “Giving up management and performance fees and handing back cash from investments managed by us is a seminal decision, however preserving client's [sic] assets is what all fund managers should put before their own interests.”

Parker expressed serious concerns about China, the US, and equity valuations in Australia. But his chief concern was property-driven household debt in Australia, saying: “When you speak to people candidly in the banks, they'll tell you very specifically that they are extraordinarily worried about the over-leverage of the Australian population in general.”

It's not just Parker who is worried. Melbourne-based funds manager JCP Investment Partners [recently warned](#)

that interest-only loans could be to Australia what sub-prime mortgages were to the US at the brink of the financial crisis. The

[RBA's increasingly urgent observation](#)

that around one-third of mortgage holders don't have a month's payment buffer is certainly

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consistent with that.

The deeper worry is that the Australian banks have been lending – both on interest-only and amortising loans – far too much as a proportion of people's incomes. I don't know if Australian banks have been overlending, but here's a little test. Suppose one puts the same post-tax income and expense variables into a big-4 bank calculator in Australia and a major national US bank. Which says you can borrow more, and by how much?

I did that exercise for a couple both earning A\$80,000 pre-tax with two children, no other debts, a modest credit card limit, and reasonable expenses. I then did the same for the same income and expense profile in the US (but in US dollars with US tax rates). Banks taking equivalent risks should lend those hypothetical couples the same amount.

The US lender would allow maximum monthly repayments of \$3,733. The Australian lender would allow \$4,709. More than 26% more.

I don't know if we have reached peak anything in Australia. But the real question is, if we have, what does the other side of the curve look like? The US petroleum data, or Hubbert's scary curve?

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